IT 02-1
Tax Type: Income Tax
Issue: Intangibles In The Sales Factor
Job Training Expense Credit (Disallowed)

STATE OF ILINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
CHICAGO, ILLINOIS

THE DEPARTMENT OF REVENUE	)	Docket No. 98-IT-0000
OF THE STATE OF ILLINOIS	)	FEIN 00-0000000
v.	)	Tax Years 1992 — 1994
"SHANGHAI, INC." ,	)	John E. White,
Taxpayer.	)	Administrative Law Judge

RECOMMENDATION FOR DISPOSITION

Appearances: Robert Denvir, Winston & Strawn, appeared for "Shanghai, Inc."; Deborah Mayer, Special Assistant Attorney General, appeared for the Illinois Department of Revenue.

Synopsis: This matter involves a Notice of Deficiency ("NOD") the Illinois Department of Revenue ("Department") issued to "Shanghai, Inc." ("Shanghai" or "taxpayer") regarding its tax years 1992 through 1994, and amended returns "Shanghai" filed for the same years. The NOD proposed to assess additional Illinois income and replacement tax after the Department determined, inter alia, that "Shanghai Trading Company, Inc." ("STCI"), "Shanghai's" foreign sales corporation, should have been included as a member of "Shanghai's" Illinois unitary business group. "Shanghai's" amended returns sought a refund for certain expenses it claimed were eligible for the training expense credit authorized by section 201(j) of the Illinois Income Tax Act ("IITA"). 35 **ILCS** 5/201(j) (*formerly* Ill. Rev. Stat. ch. 120, ¶ 2-201(*l*) (1986)) (hereinafter "§ 201(j)").

Prior to holding a pre-hearing conference, the parties filed cross-motions for partial summary judgment regarding, *inter alia*, the availability of a § 201(j) credit for what the parties referred to as Trainee Wages, which motions were, on that issue, resolved in "Shanghai's" favor. This recommendation, in addition to addressing the remaining issues, also gives effect to the Director's grant of partial summary judgment to "Shanghai" for the creditable amount of Trainee Wages paid during the years at issue.

Pursuant to a pre-hearing order, the parties agreed to the issues to be resolved at hearing. Those issues generally involve: (1) whether "STCI" was properly included in "Shanghai's" Illinois unitary business group; and (2) whether certain amounts "Shanghai" paid or accrued during the years at issue for what the parties refer to as Fringe Benefits are creditable under § 201(j) or under the income tax regulation interpreting and administering that provision. In lieu of hearing, the parties submitted a stipulation of facts and a group of stipulated exhibits. I have considered the evidence, and I am including in this recommendation findings of fact and conclusions of law. I recommend that both issues be resolved in taxpayer's favor, but that "Shanghai" not be granted a refund or credit for all of the amounts claimed as Fringe Benefits.

Statement of Facts

Facts Regarding "STCI'S" Business Operations

1. "STCI" was formed in 1984 under the laws of the Virgin Islands, a United States possession. Factual Stipulation [Regarding] Jobs Training Credit and Foreign Sales Corporation Issues (hereinafter "Stip."), ¶ 13.

2. "STCI" conducted business operations as a Foreign Sales Corporation (“FSC”) as that term is defined in § 922 of the Internal Revenue Code (the “IRC” or the “Code”). Stip. ¶ 14; *see also* 26 U.S.C. §§ 924(d), 925(c).

3. "STCI" contracted for the services required to be performed by a FSC, as contemplated by Code Sections 924(d) and 925(c). Stip. ¶ 46.

4. Because it contracted for the services it was required to perform as a FSC, "STCI" owned no tangible personal property other than its books and records, and it owned no real property. Stip. ¶ 46. It also had no employees. *Id*.

5. "STCI" maintains an office in (Someplace), the Netherlands, which "STCI" rents from "Shanghai’s Netherlands subsidiary, "Zuyder Zee, Inc." (“Zuyder”). Stip. ¶ 43; Stip. Ex. 9.

6. "Zuyder" also agreed to provide legal and accounting services to "STCI", or to arrange for others to provide those services. Stip. Ex. 10, p. 2.

7. Under the terms of a Sublease and Services Agreement between "Zuyder" and "STCI", which was in effect during the 1992-1994 tax years, "Zuyder" charged "STCI" annual rental for "STCI"’s office, related office equipment, and for legal and accounting services in the following amounts: $2,247 for 1992; $1,642 for 1993, and $2,742 for 1994. Stip. ¶ 43; Stip. Exs. 9-10.

8. The size of "STCI’s" (Someplace) office was 12.14 square meters, plus common space of 14.10 square meters. Stip. ¶ 44.

9. "STCI" maintained its books and records at its office in (Someplace), the Netherlands. Stip. ¶ 45.

10. "STCI" also kept a set of its books and records at "Shanghai's" headquarters in (Someplace), Illinois, as required under §§ 922(a)(1)(D)(iii) and 6001 of the Code. Stip. ¶ 45; 26 U.S.C. §§ 922(a)(1)(D)(iii), 6001.

11. "STCI" entered into contracts titled, "Agency Agreements" with "Shanghai" and the following "Shanghai" subsidiaries: "Shanghai Chemicals Inc." ("SCI"); "Shanghai Health Products, Inc." ("SHPI") and "Oxymoron DPR, Inc." ("OPRI"); "Shanghai Laboratories International Co." ("SLIC"); "Shanghai Manufacturing, Inc." ("SMI"); "Ike Turner Corporation" ("ITC"). Stip. ¶15; Stip. Group Exs. 1 (copies of Agency Agreements). Those Agency Agreements were in effect during the 1992-1994 tax years. Stip. ¶ 15.

12. Pursuant to the terms of those Agency Agreements, "STCI" agreed to:

- act as the agent for "Shanghai" and its subsidiaries in connection with the designated sales (the "Sales") by "Shanghai" and subsidiaries of their export property (the "Export Property"). Stip. ¶ 16; Stip Exs. 1B-1E (§ 3(a) of each Agency Agreement).
- perform activities ("Sales Activities") in furtherance of sales of Export Property by "Shanghai" and its subsidiaries that included: i) solicitation, negotiation, and making of sales contracts; ii) advertising and promotion of sales; iii) processing customer orders and arranging for delivery; iv) transportation; v) determination and transmittal of a final invoice or statement of account and receipt of payment; and vi) assumption of credit risk. Stip. ¶ 16; Stip Exs. 1B-1E (§ 3(a) of each Agency Agreement).

- perform the Sales Activities "… outside the United States in such manner, at such times, and to such extent, as Section 924(d) of the Code requires in order for all 'gross receipts' from all Sales to be treated as 'foreign trading gross receipts,' as defined in Section 924 of the Code." Stip. ¶ 17; Stip. Exs. 1B-1E (§ 3(b) of each Agency Agreement).

13. Under § 4 of the Agency Agreements, "Shanghai" and its subsidiaries agreed to pay "STCI" commissions ("Sales Commissions"), as determined under Section 925 of the Code, for Sales activities "STCI" performed in furtherance of the Sales of Export Property by "Shanghai" and its subsidiaries. Stip. ¶ 18; Stip. Exs. 1B-1E (§ 4 of each Agency Agreement).

14. "Shanghai" and its subsidiaries paid "STCI" Sales Commissions, and "STCI" reported these Sales Commissions on its federal income tax returns. Stip. ¶ 19; Stip. Exs. 2A (pp. AB000653-AB000661), 2B (pp. AB000694-AB000704), 2C (pp. AB000735-AB000747) (copies of Schedule P (Transfer Price or Commission) forms for, respectively, "STCI's" 1992-1994 federal income tax forms ("U.S. 1120 FSC")).

15. "STCI" reported its Total Sales Commissions as "foreign trading gross receipts" under § 924 of the Code. Stip. ¶ 21; Stip. Exs. 2A-2C (Schedule B (Taxable Income (Loss)) forms for, respectively, "STCI's" 1992 – 1994 federal tax forms).

16. "STCI" also entered into contracts titled, "Service Agreements" with "Shanghai" and with ACI, AHPI and OPRI (Stip. Ex. 4-B), ALIC (Stip. Ex. 4-C), AMI (Stip. Ex. 4-D), and with STC (Stip. Ex. 4-E). Stip. ¶ 22; Stip. Group Ex. 4.

17. Under § 3 of the Service Agreements, "Shanghai", "SCI", "SHPI", "OPRI", "SLIC", "SMI" and "STC" agreed to perform the Sales Activities that "STCI" was obligated to perform under Section 3 of the Agency Agreements. Stip. ¶ 23; Stip. Group Ex. 4.

18. The term “Contracting Person” is defined in § 3i of the Agency Agreements and in § 3d of the Service Agreements to mean any "STCI" affiliate that contracts, as well as any unaffiliated third party that subcontracts, to perform the Sales Activities called to be performed by the respective agreements. Stip. ¶ 23; Stip. Group Ex. 4.

19. As set forth in § 3 of the Service Agreements, obligations assumed by the Contracting Persons included "STCI’s" obligation under § 3 of the Agency Agreements to perform the Sales Activities “… outside the United States in such manner, at such times, and to such extent, as section 924(d) of the Code requires in order for ‘gross receipts’ from all Sales to be treated as ‘foreign trading gross receipts’ as defined in Code Section 924.” Stip. ¶ 23; Stip. Exs. 4B-4E (§ 3 of each Service Agreement).

20. The Sales Activities were performed by employees of "Shanghai" and its subsidiaries as well as by employees of the unaffiliated subcontractors, and were performed outside as well as within the United States. Stip. ¶ 23.

21. Under § 4 of the Service Agreements, "STCI" agreed to pay "Shanghai" and its subsidiaries compensation in the minimum amounts permitted by the principles of section 482 of the Code for the services they provided to "STCI". Stip. ¶ 24; Stip. Exs. 4B-4E (§ 4 of each Service Agreement).

22. "STCI" reported the compensation payments made to "Shanghai", its subsidiaries, and other Contracting Persons as deductions on its federal income tax returns. Stip. ¶ 25; Stip. Group Ex. 2 (Schedule G (Deductions Allocated or Apportioned to Foreign Trade Income) forms for, respectively, "STCI"'s 1992 – 1994 federal tax forms).

23. The compensation "STCI" paid to "Shanghai" and its subsidiaries for the services they performed for "STCI", pursuant to § 4 of the Service Agreements, reflects costs "Shanghai", its subsidiaries and other Contracting Persons incurred for: solicitation, negotiation, and making of sales contracts; advertising and promotion of sales; processing customer orders and arranging for delivery; transportation; determination and transmittal of a final invoice or statement of account and receipt of payment; and assumption of credit risk. Stip. ¶ 26.

24. "Shanghai" maintained books and records in which the costs it and/or its subsidiaries incurred when performing services for "STCI" pursuant to the Service Agreements are reflected. Stip. ¶ 27a-d, 28; Stip. Group Exs. 14 -15. Those books and records include trial balances which "Shanghai" kept as part of its international general ledger reporting system (Stip. ¶ 27; Stip. Group Ex. 14), and a journal entry detail, in which "Shanghai" summarized the individual journal entries made to "STCI's" cost accounts that were included in the trial balance kept pursuant to "Shanghai's" international general ledger reporting system. Stip. ¶ 29; Stip. Group Ex. 15.

25. In some instances, the entries on "Shanghai's" books and records represent expenses incurred in the performance of Sales Activities by employees of

"Shanghai" or its subsidiaries, and in other instances the entries represent expenses (e.g. freight expense) incurred for performance of the Sales Activities by other Contracting Persons. Stip. ¶ 27; Stip. Group Exs. 14-15.

26. "STCI" based its compensation to "Shanghai" and/or its subsidiaries on the costs incurred by the service providers. Stip. ¶ 27.

27. For each of the years at issue, "STCI" incurred “foreign direct costs” (as that term is used in § 924(d)(3)(B) of the Code) in the following areas: Advertising and Sales Promotion, Processing and Arranging; Transportation; Assumption of Credit Risk; and Other Deductions. Stip. ¶¶ 30-35.

28. For "STCI’s" 1992 tax year, 86% of its total direct foreign costs were incurred outside the United States and 14% within the United States. Stip. ¶ 30. For 1993, "STCI" incurred 83.9% of its total direct foreign costs outside the United States, and 16.1% inside the U.S. Stip. ¶ 32. For 1994, "STCI" incurred 84.7% of its total direct foreign costs outside the U.S., and 15.3% within the U.S. Stip. ¶ 34.

29. "STCI" maintains a bank account at Citibank in St. Thomas, the United States Virgin Islands, into which the Sales Commissions it receives and reports on its federal income tax return are regularly deposited and credited. Stip. ¶ 37; Stip. Exs. 7A (copies of Citibank bank statements), 7B copies of printouts of general ledger details regarding Citibank account), and 7C ("Shanghai" prepared summary schedules for 1992-1994).

30. "STCI’s" bank account at Citibank in the Virgin Islands was regularly debited for the following expenses: payments to "Shanghai" and its subsidiaries (including rent for "STCI’s (Someplace), Netherlands office) pursuant to § 4 of the Service

Agreements, of approximately $42 million for 1992, $41 million for 1993, and $43 million for 1994; payments of taxes totaling approximately $10 million for 1992, $ 4 million for 1993 and $7 million for 1993, which included payments of federal income taxes to the Internal Revenue Service, and payments of franchise taxes to the Virgin Islands Commissioner of Finance; and miscellaneous legal fees and bank charges. Stip. ¶ 37.

31. Four "Shanghai" employees, "J. Sprat" ("Shanghai's" Vice-President and Treasurer), "J. Horner" (Director of "Shanghai's" Domestic Treasury Operations), "P. Piper" ("Shanghai's" Vice President, Taxes) and "T. Thumb", (Director of International Taxes for "Shanghai"), had signature authority for "STCI's" bank accounts. Stip. ¶ 39.

32. Each of these four employees: had offices in (Someplace), Illinois; spent, on average, less than 1% of his time each year on activities related to this signatory authority; had offices of at least 10 feet by 10 feet; and received an average annual salary from "Shanghai" in excess of $100,000. Stip. ¶ 39. "Shanghai" allocated all expenses associated with these employees to its own account and none to "STCI". *Id*.

33. "STCI's" Board of Directors conducted their meetings in the Virgin Islands. "STCI's" Directors and their office locations were as follows:

Director	Office Location
"James Joyce"	----, Virgin Islands
"Erica Jong"	----, Virgin Islands
"Leon Uris"	----, IL
"James Agee"	----, IL
"S. Bullock" (1/l/92 - 11/23/92)	----, IL
"Andrew Johnson" (1/l/92 -4/18/94)	----, IL

Stip. ¶ 40.

34. "STCI's" officers and their office locations were as follows:

Officers, Office Held	Office Location
"Leon Uris", President	----, IL
"Peter Piper", Vice President	----, IL
"Jack Sprat", Treasurer	----, IL
"Gabriel Kaplan", Asst. Treasurer (1/l/92 - 11/92)	----, IL
"S. Bullock", Secretary	----, IL
"Sandy Koufax", Asst. Secretary	----, IL

Stip. ¶ 41.

35. Four "Shanghai" employees were responsible for monitoring the activities of "STCI" for the benefit of "Shanghai" in order to preserve "Shanghai's" federal income tax deductions attributable to "STCI's" continued status as a FSC. Stip. ¶ 47. These individuals were: "S. Gonzales", Assistant Controller, Division Accounting, "Shanghai" International Division; "T. Thumb", Director of International Taxes; "Tom Brookshire", International Tax Counsel; and "Mary Martin", International Tax Counsel. *Id*. These employees' offices are located in (Someplace), Illinois. *Id*. Each of the employees spent, on average, less than 2% of his time each year on activities related to such monitoring activity. *Id*. Each employee had an office that was at least 10 feet by 10 feet. *Id*. Each employee received an average annual salary in excess of $100,000. *Id*. "Shanghai" allocated all expenses associated with the services these employees provided to its (i.e., "Shanghai's") own account and none to "STCI". *Id*.

36. Three "Shanghai" employees who had offices in (Someplace), Illinois had responsibilities regarding the federal income tax benefits "Shanghai" recognized from its transactions with "STCI" which included preparing and filing "STCI's"

U.S. 1120 FSC. Stip. ¶ 48. Each of these three employees spent less than 5% of his time per year working for "Shanghai" calculating the tax deductible sales commissions that were paid to "STCI" and reported on "STCI's" federal income tax returns. *Id*. Each employee received average annual compensation of approximately $60,000 per year. *Id*. "Shanghai" allocated all expenses associated with their services to its own account and none to "STCI". *Id.*

37. "Shanghai" filed Illinois combined corporate income tax returns (forms IL-1120) for tax years 1992 through 1994 on which it included certain domestic subsidiaries in its unitary business group as defined by § 5/1501(a)(27) and as required by § 304(e) of the IITA. Stip. ¶ 49.

38. When preparing and filing its Illinois combined returns for 1992-1994, "Shanghai" excluded "STCI" from its unitary group. Stip. ¶ 50.

39. Since, during each of the years at issue, "STCI" had no employees, it paid no compensation to any employee during the years at issue. Stip. ¶ 46; *see also* 86 Ill. Admin. Code § 100.3360(a)(1) ("The payroll factor of the apportionment formula for each trade or business of an employer shall include the total amount paid by the employer in the regular course of its trade or business for compensation during the tax period.").

40. Thus, when determining that "STCI" should be excluded from its Illinois unitary business group under the 80/20 test, "Shanghai" used only "STCI's" applicable domestic (U.S.) and everywhere property values to measure its business activities. Stip. ¶ 50; *see also* 35 **ILCS** 5/1501(a)(27); 86 Ill. Admin. Code § 100.9700(c)(2)(B) (1990).

41. "Shanghai" calculated the denominator of "STCI's" 80/20 property fraction by multiplying by eight the net amount of rent it paid for its Netherlands office sublease. Stip. ¶¶ 9-10, 50; 86 Ill. Admin. Code § 100.3350(f)(1). Since "STCI" had no U.S. property, it calculated the numerator of its 80/20 fraction to be zero. Stip. ¶¶ 46, 50.

42. For purposes of the 80/20 test the Department counted as part of "STCI's" domestic payroll portions of the compensation "Shanghai" paid to some of its (i.e., "Shanghai's") employees for the work they performed on matters that "Shanghai" and/or its subsidiaries agreed to perform for "STCI". Department's Brief, pp. 15-18 & Addendum I thereto.

43. For purposes of the 80/20 test the Department counted as part of "STCI's" domestic property some of amounts "Shanghai" reported as being attributable to its charges to "STCI" for services "Shanghai" and/or other "Shanghai" subsidiaries performed pursuant to the Service and/or Agency Agreements. Stip. ¶¶ 15-28; Stip. Group Exs. 14-15; Department's Brief, pp. 18-20 & Addendum I thereto.

Facts Regarding The Amended Return "Shanghai" Filed To Claim Credit For Training Expenses, Pursuant To § 201(j) of the IITA

44. On February 12, 1998 "Shanghai" filed Illinois Amended Corporation Income and Replacement Tax Returns ("IL-1120-Xs") for each of the 1992-1994 tax years claiming training expense credit under 35 **ILCS** 5/201(j) for wages paid to employees while in training ("Trainee Wages"), as well for amounts paid to others regarding the time they spent in training ("Fringe Benefits"). Stip. ¶ 1.

45. On those returns, "Shanghai" reported that it paid the following amounts as “Fringe Benefits” during the years at issue: $213,751,178 for 1992; $222,349,761 for 1993; and $217,915,558 for 1994. Stip. ¶ 3.

46. Those Fringe Benefits figures represent 29.5% of "Shanghai’s" “Illinois Payroll,” which consists of the total wages, salaries, commissions and bonuses "Shanghai" paid to its employees working in Illinois. Stip. ¶ 4; *id.*, ¶¶ 2-3. "Shanghai" calculated that its Fringe Benefit amounts equaled 29.5% of its Illinois Payroll, after dividing the amount of its Total Fringe Benefits paid for its (Someplace) County, Illinois location by the amount of Annual Payroll amounts for the same location. Taxpayer’s Motion for Partial Summary Judgment (“TMSJ”), Exs. A (affidavit of "John Doe", ¶¶ 12), A-2 (schedule titled, “1991 Fringe Benefits Matrix” (row headings and column 1 entries))[1]; Department Motion for Partial

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[1] I incorporate as part of these findings of fact the undisputed facts underlying the parties’ stipulations regarding "Shanghai’s" calculation that its Fringe Benefits equal 29.5% of its Total Illinois Payroll. Specifically, I incorporate paragraph 12 of "Doe’s" affidavit (TMSJ Ex. A), which I repeat here:

> 12. For internal cost accounting control purposes personnel of "Shanghai’s" domestic tax department that report to me have determined that “fringe” benefit expenses equal 29.5% of Illinois Payroll. *See* Exhibit A-2 – "Shanghai" Schedule Computing 29.5% “Fringe” Percentage. I have reviewed their calculations and determined them to be accurate.

TMSJ Ex. A.

I also take note of the way that "Shanghai’s" tax personnel, referred to in paragraph 12 of "Doe’s" affidavit, arrived at the 29.5% figure, as demonstrated by the schedule attached as Exhibit A-2 of "Shanghai’s" motion. TMSJ Ex. A-2. The first column entries on that exhibit all refer to amounts attributable to "Shanghai’s" (Someplace) Co. Illinois operations. First, the schedule includes amounts for the following subject headings: Active Average [Employee] Population; Annual Payroll and Average Payroll per [Employee]. It next schedules and calculates Total Fringe Benefits for "Shanghai’s" (Someplace) Co. operations, by adding the sums of the amounts attributed to each of the following headings: Net Composite Insurance; Payroll Taxes; Profit Sharing; and then Stock Retirement Plan; OPEB; and Pension Plans. Then, the schedule calculates the Total Cost/Payroll (%) by dividing Total Fringe Benefits by the Annual Payroll. The quotient is 29.5%. Finally, I note the following amounts set forth in that exhibit: the column 1, row 2 amount (Annual Payroll) is 970,523; the column 1, row 4 amount (Payroll Taxes) is 75,237; and the column 1, row 12 amount (Total Fringe Benefits) is 286,356.

Summary Judgment ("DMSJ"), p. 5 ("As set forth in the parties' August 16, 1999 Agreed Order, the material facts are undisputed."); *see also* Stip. ¶¶ 4, 57.

47. The amounts the parties refer to as Fringe Benefits consist of "Shanghai's" payments for employee insurance (medical, dental and life); employee profit sharing, pension and stock retirement plans; and federal and state employer payroll taxes. Stip. ¶ 4. The "employer payroll taxes" consist of federal and state unemployment taxes and federal Social Security and Medicare taxes. Addendum to Stipulation ("Stip. Add.") ¶ 1.

48. "Shanghai" computed the jobs training credit by: (a) adding its total Illinois Payroll (consisting of wages, salaries, commissions and bonuses paid to employees working in Illinois) to Fringe Benefits; (b) multiplying that sum by a percentage reflecting the amount of time its Illinois employees spent in training (2.18% for 1992; 2.18% for 1993; and 2.57% for 1994); and (c) multiplying that product by the credit rate of 1.6%. Stip. ¶ 5; *see also* TMSJ Ex. A (¶¶ 12-15, 17-19); DMSJ, p. 5; 8/16/99 Agreed Order (¶ 7).

49. On July 31, 1998 following an audit of tax returns filed by "Shanghai" for the 1992-1994 tax years, the Department timely issued Notices of Denial denying "Shanghai's" refund claims. Stip. ¶ 6. "Shanghai" timely protested this denial and requested an administrative hearing in connection with its protest. *Id*.

50. The parties filed cross motions for partial summary judgment regarding the applicability of the type of expenses claimed on "Shanghai's" amended return to § 201(j) and/or income tax regulation 100.2150. Stip. ¶¶ 8-9.

51. As part of "Shanghai's" Motion for Partial Summary Judgment, it included the following schedule to show the amounts it claims as creditable Trainee Wages and Fringe Benefits expenses.

Tax Year	Trainee Wages	Fringe Benefits	TOTAL
1992	$ 252,154	$ 74,385	$ 326,539
1993	262,297	77,378	339,675
1993	303,595	89,560	393,155
TOTAL	$ 818,046	$ 241,323	$ 1,059,369

TMSJ Ex. A (¶ 19) (in the above table, the amount of Fringe Benefits = 29.5% of the Trainee Wages for the same year);[2] *see also* Stip. ¶¶ 8-9. The Department has never disputed the correctness of "Shanghai's" calculations of either Trainee Wages or Fringe Benefits. 8/16/99 Agreed Order; Stip. ¶¶ 12, 57.

52. Pursuant to an Agreed Order dated August 16, 1999, "Shanghai" agreed to submit to a re-audit and/or additional discovery to determine the amount of Trainee Wages and Fringe Benefits which may qualify for the credit, in the event "Shanghai" prevailed on its motion for partial summary judgment. Stip. ¶ 7; 8/16/99 Agreed Order.

53. On June 6, 2000, the Director issued a decision granting partial summary judgment for "Shanghai" on the Trainee Wages issue, stating that the Department would abandon its assertion that 86 Ill. Adm. Code § 100.2150 has only prospective application. Stip. ¶ 11. The Director's decision denied "Shanghai's" motion for

[2] While I note that the parties do not dispute the correctness of "Shanghai's" calculations of the amounts claimed to be creditable here (*see* 8/16/99 Agreed Order (¶ 7)); Stip. ¶ 57), whether it is entitled to $241,323 in training expense credits for the Fringe Benefit expenses at issue (*see* TMSJ Ex. A (¶ 19)) depends on whether all of the amounts included as Fringe Benefits may be considered creditable training expenses under § 201(j) of the IITA and/or under Department income tax regulation § 100.2150(d)(1).

partial summary judgment with respect to the issue of Fringe Benefits, and did not grant judgment to the Department on the same amounts. Stip. ¶ 11.

54. The Director's decision directed that a re-audit of the taxpayer be conducted to determine the amount of training expense credit that may be documented. Stip. ¶ 11. The Director further remanded the case for a determination of the amount of compensation that is an expense eligible for the jobs training credit consistent with the definition of that term under 35 **ILCS** 5/1501(a)(3). *Id*.

55. Prior to the time that the Director's decision was issued, the Administrative Law Judge ("ALJ") requested that the Department determine whether a re-audit would be necessary in the event "Shanghai" prevailed on both issues. Stip. ¶ 12. The Department examined its audit schedules and determined that no on-site re-audit was necessary. *Id*.; *see also* 5/8/00 Order.

Conclusions of Law:

The Department established the prima facie correctness of its determinations when it introduced the NOD and denial into evidence. Stip. Exs. 12-13; 35 **ILCS** 5/904, 5/910. Thereafter, the burden shifted to "Shanghai" to prove that the Department's determination that "STCI" should be included in "Shanghai's" unitary group was in error. 35 **ILCS** 5/904(a); Balla v. Department of Revenue, 96 Ill. App. 3d 293, 295, 421 N.E.2d 236, 238 (1st Dist. 1981). "Shanghai" also has the burden to establish that the amounts the parties refer to as Fringe Benefits are creditable training expenses, under § 201(j) of the IITA. Balla, 96 Ill. App. 3d at 296, 421 N.E.2d at 238 ("… when a taxpayer claims that he is exempt from a particular tax, or where he seeks to take advantage of deductions or credits allowed by statute, the burden of proof is on the taxpayer.") (*citing* Telco Leasing, Inc. v.

Allphin, 63 Ill. 2d 305, 347 N.E.2d 729 (1976)); Bodine Electric Co. v. Allphin, 81 Ill. 2d 502, 410 N.E.2d 828 (1980)).

80/20 Issue[3]

This issue requires an examination of the Illinois income tax statutes and regulations that describe how to determine whether a person must be excluded from a unitary business group because it conducts 80% or more of its total business activities outside the water's edge of the United States. The examination begins by a review of the definition of a unitary business group in § 1501(a)(27) of the IITA. That section provides:

> (27) Unitary business group. The term "unitary business group" means a group of persons related through common ownership whose business activities are integrated with, dependent upon and contribute to each other. ***The group will not include those members whose business activity outside the United States is 80% or more of any such member's total business activity; for purposes of this paragraph and clause (a)(3)(B)(ii) of Section 304, business activity within the United States shall be measured by means of the factors ordinarily applicable under subsections (a), (b), (c), (d), or (h) of Section 304 except that, in the case of members ordinarily required to apportion business income by means of the 3 factor formula of property, payroll and sales specified in subsection (a) of Section 304, including the formula as weighted in subsection (h) of Section 304, such members shall not use the sales factor in the computation and the results of the property and payroll factor computations of subsection (a) of Section 304 shall be divided by 2 (by one if either the property or payroll factor has a denominator of zero). The computation required by the preceding sentence shall, in each case, involve the division of the member's property, payroll, or revenue miles in the United States, insurance premiums on property or risk in the United States, or financial organization business income from sources within the United States, as the case***

[3] The parties refer to this issue as the FSC Issue (*see* Stip. ¶ 50), although the 80/20 test applies to all persons, and not just to persons who conduct business as foreign sales corporations. *See* 35 **ILCS** 5/1501(a)(27).

> ***may be, by the respective worldwide figures for such items.*** ***

35 **ILCS** 5/1501(a)(27) (emphasis added).

The 80/20 determination is required to effect the Illinois General Assembly's intent to create Illinois' scheme of water's edge combined reporting for related persons who conduct a single unitary business. 35 **ILCS** 5/304(e); General Telephone Co. v. Johnson, 103 Ill. 2d 363, 372-73, 469 N.E.2d 1067, 1072 (1984). Pursuant to its statutory authority (35 **ILCS** 5/1401(a)), the Department promulgated regulations to administer and enforce the General Assembly's definition of a unitary business group in § 1501(a)(27). 86 Ill. Admin. Code §§ 100.3350, 100.3360, 100.9700. Those regulations further illustrate how an 80/20 determination is to be made, and what a person's payroll and property factors are supposed to measure. Specifically, regulation § 100.9700(c) provides:

> (c) The 80-20 U.S. business activity test for prospective members. The factors to be used in determining whether 80% or more of a person's business activity is conducted outside the United States shall be gross figures without eliminations premised on the person's membership in any unitary business group. However, the factors should relate to the common accounting period, as defined in Section 100.3310, of the unitary business group of which the person being tested could become a member were the person's business activity found to be less than 80% outside the United States. The factors to be used are as follows:
>
> 1) persons required to apportion business income under IITA Section 304(a) will use property and payroll,
> 2) persons required to apportion business income under IITA Sections 304(b), 304(c) or 304(d) will use the respective factors prescribed in those provisions.
>
> A) In accordance with IITA Section 102 and 26 USC 7701(b)(9), the phrase "United States" as used in IITA Section 1501(a)(27) shall include only the fifty states and the District of Columbia.

> B) Mechanically, the computation of the 80-20 U.S. business activity test requires the formation of one or two fractions, as the case may be, and the subsequent averaging of those fractions to arrive at an overall U.S. business activity in relation to world-wide business activity. The numerators of the fraction represents U.S. property, U.S. payroll, U.S. revenue miles, insurance premiums on property or risk in the U.S. or financial organization business income from sources within the U.S.; the respective denominators are world-wide figures.
>
> ***

86 Ill. Admin. Code § 100.9700(c).

When using the 80/20 test in this matter, therefore, the first step requires a determination whether the denominator of "STCI's" payroll factor is zero. 35 **ILCS** 5/1501(a)(27). If so, "STCI's" business activities must be measured using only a property factor; if not, its business activities must be measured using both payroll and property. *Id.*; 86 Ill. Admin. Code § 100.9700(c)(2)(B).

On this point, "Shanghai" argues that "STCI" had no payroll factor, since it is undisputed that "STCI" had no employees during the years at issue. Taxpayer's Initial Brief ("'Shanghai's" Brief"), pp. 8-9; Stip. ¶ 46. Despite its stipulation that "STCI" had no employees, however, the Department argues that when determining whether 80% or more of "STCI's" total business activities are conducted outside the water's edge, it is proper to "reallocate" to "STCI" a portion of the compensation "Shanghai" paid to *its* employees who worked within the United States, for the small amount of time any such employees performed work for "Shanghai" on activities "Shanghai" agreed to perform for "STCI", and for which "STCI" agreed to compensate "Shanghai". *See* Department Brief, pp. 2, 15-18, 30-31 & Appendix I thereto. The Department also asserts that "STCI's" officers must be considered its employees, by operation of law. *Id.*, pp. 2, 15-18.

To support its argument that some of the compensation others paid to "STCI's" officers and to "Shanghai's" and/or its subsidiaries' employees should be reallocated to "STCI" when performing the 80/20 test, the Department cites to § 3121(d) of the Code (*see* Department's Brief, p. 15), which defines the term "employee" for purposes of Chapter 21 of the Code. 26 U.S.C. § 3121(d). Chapter 21 of the Code is titled "Federal Insurance Contributions Act," and different sections of that chapter impose taxes on the wages of employed individuals, and on employers, to fund federal Social Security and Medicare programs. 26 U.S.C §§ 3101(a)-(b) (taxes imposed on employees), 3111(a)-(b) (taxes imposed on employers). Section 3121(d) provides, in pertinent part:

> (d) Employee.
> For purposes of this chapter, the term "employee" means—
> (1) any officer of a corporation; …
> ***
> if the contract of service contemplates that substantially all of such services are to be performed personally by such individual; ***except that an individual shall not be included in the term "employee" under the provisions of this paragraph*** if such individual has a substantial investment in facilities used in connection with the performance of such services (other than in facilities for transportation), or ***if the services are in the nature of a single transaction not part of a continuing relationship with the person for whom the services are performed***; …
> ***

26 U.S.C. § 3121(d) (emphasis added).

The Department next quotes part of an applicable Treasury Regulation in which the Internal Revenue Service interprets § 3401 of the Code. Department Brief, p. 15 (*citing* 26 CFR § 31.3401(c)-1). The complete text of that regulation provides:

> (a) The term "employee" includes every individual performing services ***if the relationship between him and the person for whom he performs such services is the legal relationship of employer and employee***. The term

includes officers and employees, whether elected or appointed, of the United States, a State, Territory, Puerto Rico, or any political subdivision thereof, or the District of Columbia, or any agency or instrumentality of any one or more of the foregoing.

(b) Generally the relationship of employer and employee exists when the person for whom services are performed has the right to control and direct the individual who performs the services, not only as to the result to be accomplished by the work but also as to the details and means by which that result is accomplished. That is, an employee is subject to the will and control of the employer not only as to what shall be done but how it shall be done. In this connection, it is not necessary that the employer actually direct or control the manner in which the services are performed; it is sufficient if he has the right to do so. The right to discharge is also an important factor indicating that the person possessing that right is an employer. Other factors characteristic of an employer, but not necessarily present in every case, are the furnishing of tools and the furnishing of a place to work to the individual who performs the services. In general, if an individual is subject to the control or direction of another merely as to the result to be accomplished by the work and not as to the means and methods for accomplishing the result, he is not an employee.

(c) Generally, physicians, lawyers, dentists, veterinarians, contractors, subcontractors, public stenographers, auctioneers, and others who follow an independent trade, business, or profession, in which they offer their services to the public, are not employees.

(d) Whether the relationship of employer and employee exists will in doubtful cases be determined upon an examination of the particular facts of each case.

(e) If the relationship of employer and employee exists, the designation or description of the relationship by the parties as anything other than that of employer and employee is immaterial. Thus, if such relationship exists, it is of no consequence that the employee is designated as a partner, co-adventurer, agent, independent contractor, or the like.

(f) All classes or grades of employees are included within the relationship of employer and employee. Thus, superintendents, managers, and other supervisory personnel are employees. ***Generally, an officer of a corporation is an employee of the corporation. However,***

> ***an officer of a corporation who as such does not perform any services or performs only minor services and who neither receives nor is entitled to receive, directly or indirectly, any remuneration is not considered to be an employee of the corporation.*** A director of a corporation in his capacity as such is not an employee of the corporation.
>
> (g) The term "employee" includes every individual who receives a supplemental unemployment compensation benefit which is treated under paragraph (b)(14) of §31.3401(a)-1 as if it were wages.
>
> (h) Although an individual may be an employee under this section, his services may be of such a nature, or performed under such circumstances, that the remuneration paid for such services does not constitute wages within the meaning of section 3401(a).

26 CFR § 31.3401(c)-1 (emphasis added).

Here, I agree with "Shanghai" that there is nothing within either the Code or the Treasury Regulation cited by the Department that requires me to treat "Shanghai's" employees as "STCI's employees, or that requires me to treat portions of the compensation "Shanghai" pays to some of its employees as part of "STCI's" domestic payroll. *See* "Shanghai's" Reply Brief ("'Shanghai's" Reply"), 2-3. In fact, a full reading of those provisions shows that federal law does not transform "Shanghai's" employees into "STCI's" employees merely because they perform minor services for "STCI" for which their employer — "Shanghai" — is paid. 26 CFR § 31.3401(c)-1(f) ("… an officer of a corporation who … performs only minor services and who neither receives nor is entitled to receive, directly or indirectly, any remuneration is not considered to be an employee of the corporation"). "Shanghai", and not the individual employees, agreed to perform services for "STCI". *Id*.

Most importantly, the Treasury Regulation the Department relies on begins its definition of "employee" with this sentence: "The term 'employee' includes every

individual performing services *if the relationship between him and the person for whom he performs such services is the legal relationship of employer and employee*." 26 CFR § 31.3401(c)-1(a) (emphasis added). The parties' stipulation shows that, as a matter of fact, the required employer-employee relationship does not exist between "STCI" and the individuals who perform services for it. Stip. ¶ 46. A stipulation of fact is a judicial admission. Keeven v. City of Highland, 294 Ill. App. 3d 345, 348, 689 N.E.2d 658, 661 (5th Dist. 1998). It is well settled in Illinois that a party can make a judicial admission that conclusively precludes assertion of a contrary position. Dayan v. McDonald's Corp., 125 Ill. App. 3d 972, 983, 466 N.E.2d 958, 967 (1st Dist. 1984) (*citing* Tolbird v. Howard, 43 Ill. 2d 357, 362, 253 N.E.2d 444 (1969)). Here, even though it has stipulated that "STCI" had no employees (Stip. ¶ 46), the Department argues that two of "STCI's" officers, and other "Shanghai" employees, were "STCI's" employees. Department's Brief, pp. 2, 15-18. At best, the Department's argument is contradicted by the stipulated facts, and is, therefore, not persuasive; at worst, its own stipulation precludes it from even making the argument. Dayan, 125 Ill. App. 3d at 983, 466 N.E.2d at 967.

The Department has also not shown how the IITA or applicable income tax regulations support its argument that, when determining whether 80% or more of "STCI's" total business activities are conducted outside the water's edge of the United States, some of "Shanghai's" payroll should be reallocated to "STCI". None of the Department's regulations promulgated to interpret the IITA's terms "unitary business group" or "payroll" expressly authorize the reallocation the Department proposes here. The payroll factor, moreover, is designed to measure "… the total amount paid by the employer in the regular course of its trade or business for compensation during the tax period." 86 Ill. Admin.

Code § 100.3360(a)(1) (emphasis added); *see also* 35 **ILCS** 5/304(a)(2). Thus, when performing the 80/20 test, it is the compensation "STCI" paid to *its* employees — and not the compensation "Shanghai" paid to its employees — that must be considered.

After acknowledging the effect of Illinois law regarding the 80/20 test and the payroll factor, I must also accept the natural consequence of the parties' stipulation that "STCI" had no employees. Stip. ¶ 46. Since "STCI" had no employees, it paid nothing in the regular course of its trade or business for compensation. *See* 86 Ill. Admin. Code § 100.3360(a)(1). Thus, "STCI's" payroll factor denominator equals zero, and its business activities must be measured using only a property factor. 35 **ILCS** 5/1501(a)(27).

With regard to the property factor, the parties also stipulate that during the years at issue, "STCI" rented an office from "Zuyder", "Shanghai's" Netherlands subsidiary, pursuant to a written Sublease and Services Agreement. Stip. ¶ 43. "STCI's" office was located in (Someplace), The Netherlands. *Id.*; Stip. Ex. 9. There can be no doubt, therefore, that "STCI" had foreign property expenses that must be included in the property factor denominator. 35 **ILCS** 5/1501(a)(27); 86 Ill. Admin. Code § 100.9700(c)(2)(B). The parties, however, dispute whether "STCI" also had domestic business activities that were measurable by the value of real or tangible property "STCI" owned or rented and used in the regular course of its trade or business conducted within the water's edge of the United States. "Shanghai" claims "STCI" had no such U.S.-based property ("Shanghai's" Brief, pp. 8-9), whereas the Department claims it did. Department's Brief, pp. 18-20, 31.

"Shanghai's" argument again has the distinct benefit of being supported by the stipulated facts and by the documents made part of this stipulated record. To begin, the parties stipulated that, other than its corporate books and records, "STCI" owned no real or

tangible personal property during the years at issue. Stip. ¶ 46. They also stipulated that "STCI" entered into contracts with others to perform the activities "STCI" was required to perform as a FSC. Stip. ¶¶ 15-18, 22-26. The stipulated facts and documents show that "STCI" was a corporation that was qualified to act, and which, in fact, conducted business as a FSC. Stip. ¶ 14; Stip. Group Ex. 2. In each of its federal income tax returns filed for the years at issue, "STCI" checked the "no" box in response to the question whether it "… at any time during the tax year engaged in a trade or business in the U.S." Stip. Ex. 2A, p. AB000647; Stip. Ex. 2B, p. AB000689; Stip. Ex. 2C, p. AB000730 (Additional Information section, line 3 (of each return)).

Despite its stipulation to those facts and documents, the Department argues that when determining whether 80% or more of "STCI's" total business activities are conducted outside the water's edge, it is proper to reallocate to "STCI" some of the value of the property "Shanghai" and/or other "Shanghai" subsidiaries either rented or owned inside the water's edge of the United States, and which they used when performing services for "STCI". Department's Brief, pp 18-20. The Department, in particular, treats as "STCI's" domestic property certain rents that "Shanghai" and/or its subsidiaries paid (or received, *see* Taxpayer's Reply, p. 4 n.1), regarding a warehouse in (Someplace), Louisiana. Department's Brief, pp. 18-19 & Appendix I thereto, pp. 2, 5. It also claims that part of the value of "Shanghai's" North Chicago, Illinois office space should be considered "STCI's" domestic real property for purposes of the 80/20 test, because that is where certain "Shanghai" employees performed services on "STCI's" behalf, and where "STCI" kept a second set of its books and records. Department's Brief, pp. 18-19. More generally, the Department treats as "STCI's" domestic property whatever costs it considers related to

the value of the real and/or tangible personal property used by "Shanghai" and/or by its subsidiaries when they provided services to "STCI" pursuant to the Service and Agency Agreements. Department's Brief, pp. 18-20 (citing entries made on schedules set forth in Appendix I thereto, pp. 2-5, which entries, in turn, were drawn from "Shanghai's" books and records set forth as Stip. Group Exs. 14-15), 31[4] & Appendix I thereto.

As was the case with the payroll factor, however, the Department's reallocation of "Shanghai's" property to "STCI" for purposes of the 80/20 test is similarly inconsistent with the definition and purpose of the property factor, as set forth in §§ 304(a)(1) and 1501(a)(27) of the IITA. Section 304(a)(1) of the IITA defines the property factor as:

> … a fraction, the numerator of which is the average value of the person's real and tangible personal property owned or rented and used in the trade or business in this State during the taxable year and the denominator of which is the average value of all the person's real and tangible personal property owned or rented and used in the trade or business during the taxable year.

35 **ILCS** 5/304(a)(1).

The Department's income tax regulation promulgated regarding § 304(a)'s definition and use of the term "property factor" confirms that the factor is supposed to

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[4] The Department supports its property reallocation, in part, as follows:

> … the 'mechanics of [its] reallocation' [is] based upon the US 1120FSC Schedule G back up, namely the cost of the services that "Shanghai" and its affiliates render to the FSC which nets the payroll and property factors. … The property is valued at 8 times the annual rent per the Illinois Tax Act. … "STCI" automatically has property because of the actual rent expense in the United States (far in excess of what is paid in the Netherlands); because of the books and records located in Illinois; because the officers and employees who worked on "STCI's" activities occupy space at "Shanghai's" headquarters, and because other tangible property was used to conduct "STCI's" activities, printing, etc.

Department Brief, p. 31.

measure the value of property that is owned or rented by the person whose business income is being apportioned, and not the value of property that is owned or rented by some other person. Income tax regulation § 100.3350(a) provides:

> In general. The property factor of the apportionment formula for each trade or business of a person shall include ***all real and tangible personal property owned or rented by such person*** and used during the tax period in the regular course of such trade or business. The term "real and tangible personal property" includes land, building, machinery, stocks of goods, equipment, and other real and tangible personal property but does not include coin or currency. Property used in connection with the production of nonbusiness income shall be excluded from the property factor. Property used both in the regular course of a person's trade or business and in the production of nonbusiness income shall be included in the factor only to the extent the property is used in the regular course of the person's trade or business. The method of determining that portion of the value to be included in the factor will depend on the facts of each case. The property factor shall include the average value of property includable in the factor. See subsection (g), below.

86 Ill. Admin. Code § 100.3350(a) (emphasis added).

Other parts of the same regulation corroborate that conclusion. For example, § 100.3350(d)-(f) provides, in part:

> (d) Numerator. The numerator of the property factor shall include the average value of the real and tangible personal property ***owned or rented by the person*** and used in this State during the tax period in the regular course of the trade or business of the person. ***
>
> ***
>
> (e) Valuation of owned property. Property ***owned by the person*** shall be valued at its original cost. ***
>
> ***
>
> (f) Valuation of rented property
>
> (1) Property ***rented by the person*** is valued at eight times the net annual rental rate. The net annual rental rate for any item of rented property is the ***annual rental rate paid by the person for such property***, less the

> aggregate annual subrental rates paid ***by subtenants of the person***. ***

86 Ill. Admin. Code § 100.3350(d)-(e) (emphasis added).

For purposes of the 80/20 test, "STCI" is “the person” or “the member” whose domestic versus worldwide property values should be compared when determining whether it may be included within, or must be excluded from, "Shanghai's" Illinois unitary business group. 35 **ILCS** 5/1501(a)(27) (“… The [80/20] computation … shall, in each case, involve the division of *the member’s* property, payroll, or revenue miles in the United States, … by the respective worldwide figures for such items. ***”) (emphasis added). The Department knows and concedes that, other than its books and records, "STCI" owned no real or tangible personal property during the years at issue. Stip. ¶ 46. Further, no part of the applicable statutes or the Department’s regulations indicates that, for purposes of apportioning business income or when performing the 80/20 test, the General Assembly intended the Department to consider the value of a person’s books and records when measuring the value of the real or tangible personal property that the person owned and used in the regular course of its trade or business. 35 **ILCS** 304(a)(1), 5/1501(a)(27); 86 Ill. Admin. Code §§ 100.3350(b), (e) (and examples cited therein), 100.9700(c)(2)(B). Since "STCI" owned no real or tangible personal property during the years at issue, the value of the property that "STCI" owned and used during the regular course of its trade or business within the water’s edge of the United States during the years at issue is zero. Stip. ¶ 46; 35 **ILCS** 304(a)(1), 5/1501(a)(27).

This record is also devoid of any evidence that "STCI" rented any real or tangible personal property that was situated within the water’s edge of the United States during the years at issue. Although the Department argues that "STCI" should be deemed to have

rented and used such property (*see* Department's Brief, pp. 18-20, 31), our supreme court has held that:

> … Rent is given in consideration of a lease. As we have already stated, a lease gives rise to the landlord-tenant relationship. In order to establish the relation of landlord- and tenant, the possession and control or the right thereto of the property must pass to the tenant.

Midland Management Co. v. Helgason, 158 Ill. 2d 98, 105, 630 N.E.2d 836, 840 (1994). Another Illinois court has held that, "[r]ent is compensation paid for the use of land, and what the tenant pays rent for is quiet enjoyment or beneficial enjoyment." Application of Rosewell, 69 Ill. App. 3d 996, 1002, 387 N.E.2d 866, 870 (1st Dist. 1979); *see also* 810 **ILCS** 5/2A-103(1)(j)-(n), (p) (statutory definitions of the terms used in Article 2A of Illinois' Commercial Code, pertaining to leases of goods).

Here, however, no provision expressed in any of the Service or Agency Agreements evinces any mutual agreement, either express or implied, that "Shanghai" or others were supposed to rent real or tangible personal property within the United States on "STCI's" behalf. Stip. Group Exs. 1, 4. The Department, moreover, has cited to no authority for the proposition that where A hires B to perform services for it, A should be understood to be "renting" or "leasing" whatever property B uses when performing such services. Without some authority grounded in fact or law, the Department should not be able to treat those agreements as though they were rental agreements in disguise. Midland Management Co., 158 Ill. 2d at 103-04, 630 N.E.2d at 839 ("Whenever there is a contract its terms must control the rights of the parties. *** … The principal function of the court in construing a lease is to give effect to the intention of the parties as expressed in the language of the document when read as a whole.").

Thus, the stipulated facts and documents included in this record do not support the Department's argument that "STCI" rented — or should be deemed to have rented — the real and tangible personal property "Shanghai" and others used when providing services for "STCI". *See* Department's Brief, pp. 18-20, 31; "Shanghai's" Reply, pp. 1, 3-4. More importantly, and absent the circumstances set forth in either §§ 304(f) or 404 of the IITA, there is nothing in the IITA's 80/20 test that grants the authority to reallocate to one person payroll or property that is properly allocable to another person. 35 **ILCS** 5/304(f), 5/404, 5/1501(a)(27). None of the circumstances described in those provisions has been shown to exist here, and the argument was never even raised.

I conclude that none of the compensation "STCI" paid to "Shanghai" and others should be reallocated as, or otherwise deemed to be equal to, the rental value of the real or tangible personal property "STCI" used in the regular course of its trade or business within the water's edge of the United States. 35 **ILCS** 5/304(a)(1); 5/1501(a)(27). This stipulated record, in fact, supports a determination that "STCI" never engaged in any trade or business within the United States during the years at issue. Stip. ¶ 14; Stip. Ex. 2A, p. AB000647; Stip. Ex. 2B, p. AB000689; Stip. Ex. 2C, p. AB000730.

The only evidence of "STCI's" property in this record is the evidence of its foreign rental property, as reflected by its sublease of an office in (Someplace), The Netherlands, and its rental payments therefor. Stip. Exs. 9-10. Thus, when using the 80/20 test to determine the amount of "STCI's" total business activities during each of the years at issue, the property fractions are as follows:

80/20 Test for 1992

U.S. property / property everywhere	$ 0 / $ 17,976	=	more than 80% of "STCI's" total business activities conducted outside the water's edge

80/20 Test for 1993

U.S. property / property everywhere	$ 0 / $ 13,136	=	more than 80% of "STCI's" total business activities conducted outside the water's edge

80/20 Test for 1994

U.S. property / property everywhere	$ 0 / $ 21,936	=	more than 80% of "STCI's" total business activities conducted outside the water's edge

Stip. ¶ 43; Stip. Exs. 9-10; 35 **ILCS** 5/1501(a)(27); 86 Ill. Admin. Code §§ 100.3350(a)(1) ("Property rented by the person is valued at eight times the net annual rental rate"), 100.9700(c)(2)(B).

After using the formula prescribed in § 1501(a)(27), I conclude the evidence shows that, for each year at issue, "STCI" conducted more than 80% of its total business activities outside the water's edge of the United States. Stip. ¶¶ 14-28, 30, 32, 34, 37, 40, 43, 45-46; Stip. Ex. 2A, p. AB000647; Stip. Ex. 2B, p. AB000689; Stip. Ex. 2C, p. AB000730; 35 **ILCS** 5/1501(a)(27); 86 Ill. Admin. Code § 100.9700(c)(2)(B). Thus, under the plain text of § 1501(a)(27), "STCI" must be excluded from "Shanghai's" Illinois unitary business group. 35 **ILCS** 5/1501(a)(27).

Training Expense Credit Issue

This issue involves expenses "Shanghai" paid or accrued for: employee insurance (medical, dental and life); employee profit sharing, pension and stock retirement plans; and "Shanghai's" federal and state employer payroll taxes that were attributable to the days, weeks, or other periods during which its Illinois resident employees, or its employees who worked in Illinois, spent in qualified training. Stip. ¶ 4; Stip. Add. ¶ 1. Since this matter was submitted as a stipulated case, with no disputed facts, it is also important to identify what is not at issue.

The Department does not dispute, and has never disputed, that the amounts each party refers to as Fringe Benefits accurately identify the proportionate amount of "Shanghai's" total payroll expenses that "Shanghai" paid for the amount of time "Shanghai's" eligible employees spent in eligible training programs. Stip. ¶¶ 1, 3-12; Department's Brief, pp. 32-34; *see also* DMSJ, p. 5 ("As set forth in the parties' August 16, 1999 Agreed Order, the material facts are undisputed."); 8/16/99 Agreed Order (¶ 7). Nor does it factually dispute, or has it ever disputed, that "Shanghai" deducted the amounts claimed as being creditable expenses from gross receipts when calculating taxable income. Stip. ¶¶ 1, 3-12; Department's Brief, pp. 32-34; 8/16/99 Agreed Order (¶ 7). The Director, in fact, granted "Shanghai's" motion for summary judgment for the amount of compensation that "Shanghai" paid to the same employees who attended the same training programs. Stip. ¶¶ 7-12. Finally, the Department determined that it needed no further review or reaudit of "Shanghai's" books and records, either before or after the Director's ruling was issued regarding the parties cross-motions for summary judgment. Stip. ¶ 12.

Thus, the parties have always agreed that the issue requires a conclusion whether the particular expenses "Shanghai" paid were creditable under § 201(j) of the IITA, or under income tax regulation § 100.2150, and not a conclusion to determine whether "Shanghai" has, in fact, established: that it spent the amounts reported in the manner claimed; that the training programs were eligible for credit; or that the amounts "Shanghai" paid were, in fact, deducted when "Shanghai" calculated taxable income. Stip. ¶¶ 1, 3-12; "Shanghai's" Brief, pp. 4-5; Department's Brief, pp. 32-34. I will now address the applicable statute and regulation, the parties' respective arguments, and then, the particular expenses at issue.

The first place to look to determine whether the particular expenses are creditable under § 201(j) is the text of the statute itself. Section 201(j) provides:

> Training expense credit. Beginning with tax years ending on or after December 31, 1986, a taxpayer shall be allowed a credit against the tax imposed by subsection (a) and (b) under this Section for all amounts paid or accrued, on behalf of all persons employed by the taxpayer in Illinois or Illinois residents employed outside of Illinois by a taxpayer, for educational or vocational training in semi-technical or technical fields or semi-skilled or skilled fields, which were deducted from gross income in the computation of taxable income. The credit against the tax imposed by subsections (a) and (b) shall be 1.6% of such training expenses. For partners and for shareholders of subchapter S corporations, there shall be allowed a credit under this subsection (l) to be determined in accordance with the determination of income and distributive share of income under Sections 702 and 704 and subchapter S of the Internal Revenue Code.
>
> Any credit which is unused in the year the credit is earned may be carried forward to each of the 5 taxable years following the year for which the credit is first computed until it is used. This credit shall be applied first to the earliest year for which there is a liability. If there is a credit under this subsection from more than one tax year that is available to offset a liability the earliest credit arising under this subsection shall be applied first.

35 **ILCS** 5/201(j) (*formerly* Ill. Rev. Stat. ch. 120, ¶ 201(*l*) (1987)).

In March 1995, the Department adopted an income tax regulation in which it described how it interpreted § 201(j), and how it would administer that provision. 19 Ill. Reg. 5824 (April 14, 1995); 86 Ill. Admin. Code § 100.2150 (1995). For purposes of this dispute, the most pertinent part of that regulation is the part that illustrates expenses the Department will consider to either qualify or not qualify for the credit. 86 Ill. Admin Code § 100.2150(d). That part of the regulation provides:

> d) Only amounts expended for eligible training will qualify as eligible training expenses. Such costs may or may not constitute "direct expenses" as that term is used in

normal accounting parlance. Capitalized costs will not qualify for the credit. However, as noted below, depreciation expenses associated with capital expenditures may qualify for the credit. The term "compensation" used in this Section is defined in IITA Section 1501(a)(3).

1) The following costs qualify as eligible training expenses:

A) Compensation of employees for time spent in training others in in-house training will qualify as eligible training expenses, but the compensation must be pro-rated based on the amount of time actually spent in conducting the training.

B) Compensation of an employee for time spent in preparing for in-house training as or for an instructor will qualify because such compensation is an expense of the training.

C) Compensation of an employee for time spent in training will qualify for the credit.

D) The cost of materials (i.e., slides, hand-outs, etc.) for in-house training will qualify for the credit because such costs are expenses of the training.

E) Pro-rata rent of a training facility is an expense eligible for the credit. Similarly, depreciation expenses for a training facility owned by a taxpayer or for equipment used for training are eligible expenses.

F) Costs of registration (including allocable wages of employees performing the registration) with state, federal or industry authorities may be eligible expenses, if such costs are related to eligible training.

G) Tuition reimbursement is an eligible expense provided that the tuition amounts were deducted in determining the employer's federal taxable income.

H) Costs of travel and lodging for eligible training provided that the costs were deducted in determining the employer's federal taxable income.

2) The following costs do not qualify as eligible training expenses:

A) The cost of the training facility and equipment is not an eligible expense. Capital costs are not eligible for the credit. However, as noted above, depreciation expense is eligible.

B) Compensation of an employee for "down time" spent informally training (i.e., a mechanic with no machinery on which to work reading about new equipment, or a mechanic reading about specifications

> of equipment never before encountered) is not an eligible expense.
>
> C) Compensation of an employee for time spent supervising another employee is not an eligible expense. For instance, a supervisor spending an hour a day reviewing and discussing a new employee's progress and planning the new employee's future work schedule would not be an eligible expense.
>
> D) Cost of a meal (breakfast or lunch) provided in the course of a brief training session is not an eligible expense. Similarly, the cost of meals provided to an employee during an all-day training session is not an eligible expense.

86 Ill. Admin Code § 100.2150(d) (1995).

"Shanghai" makes two arguments in favor of its claim. The first is that the expenses at issue constitute "compensation" under the Department regulation interpreting that term. "Shanghai's" Brief, p. 4. It next argues that the expenses are creditable under the plain text of § 201(j), because they represent some of the "'amounts [that it] … paid *or* accrued, *on behalf of* …' employees in training." *Id*. (emphasis original). Specifically, "Shanghai" argues that "[i]t would be improper to interpret … [the Department's applicable] regulation more narrowly than the scope of the credit provided by the statutory language of Act Section 201(j)." *Id*., pp. 4-5 (*citing* DuMont Ventilating Co. v. Department of Revenue, 73 Ill. 2d 243, 383 N.E.2d 197 (1978)). Thus, "Shanghai" claims credit for the expenses at issue based on the text of the statute itself, and not solely based on the Department's more recent interpretation of that provision.

In its response, the Department argues that since the expenses at issue were not paid *to* the employees who took part in eligible training, the expenses do not meet the definition of compensation. Department's Brief, pp. 32-34. That particular position is also set forth in a September 2000 informational bulletin issued by the Department titled,

"Training Expense Credit Update", a copy of which the Department appended to its brief. *Id*. p. 33 & Appendix IV thereto.[5] Further, the Department implies that it never intended to interpret § 201(j) to include costs such as the ones at issue here as creditable training expenses, because "… nowhere in the regulation is there any mention of 'fringe benefits.'" *Id*. p. 33.

The Department's first argument, that the expenses are not creditable because they were not paid to the employees who took eligible training, and thus do not constitute "compensation" as that term is defined in another Department income tax regulation, seems to assume that the only creditable training expenses are those that constitute compensation. The Department's own regulation dashes that assumption, since it lists expenses other than compensation that will also qualify for the credit. Specifically, amounts paid for materials used for in-house training, pro-rata rent of a training facility, costs of registration with state, federal or industry authorities, and costs of travel and lodging for eligible training are also not amounts that will be paid to eligible employees, yet each of those costs qualifies for the credit. 86 Ill. Admin. Code § 100.2150 (d)(1)(D)-(F), (H). Merely arguing that the amounts at issue are not compensation, therefore, does not effectively counter "Shanghai's" argument that the expenses at issue are creditable under the plain text of § 201(j). "Shanghai's" Brief, pp. 4-5.

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[5] The bulletin includes the following statements:

> We also have received inquiries concerning whether employee benefits provided for employees involved in training may qualify for the credit.
>
> Employee benefits do not qualify for the Training Expense Credit. The regulation[ ] provides that "compensation" qualifies for the credit if it falls within the meaning of wages, salaries, commissions, and any other form of personal services" as stated in the Illinois Income Tax Act.

Department's Brief, Appendix IV thereto.

The Department's next argument, that the expenses at issue in this case cannot be considered creditable training expenses since the phrase "fringe benefits" is not mentioned within the regulation, can easily be turned on its head. Specifically, the absence of the phrase "fringe benefits" from the regulation's list of nonqualifying costs might reasonably be interpreted as the Department's concession that such expenses might qualify. The better way to view the absence of the phrase from the regulation, I believe, is to recognize that the pertinent regulation does not identify, nor could it possibly identify, all of the possible expenses that might form the basis of a claim for credit for "… ***all*** amounts paid or accrued, on behalf of all persons employed by the taxpayer in Illinois or Illinois residents employed outside of Illinois by a taxpayer, for educational or vocational training in semi-technical or technical fields or semi-skilled or skilled fields, which were deducted from gross income in the computation of taxable income." 35 **ILCS** 5/201(j) (emphasis added).

To my knowledge, moreover, the Department has never described its regulation's lists of qualifying and nonqualifying expenses as being collectively exhaustive. *See* 86 Ill. Admin. Code § 100.2150. And where the Department intends such a list to be exhaustive, it plainly says so. *E.g.*, 86 Ill. Admin. Code §§ 100.2470(c) ("… Following is a list (intended to be exhaustive) of exempt income and the specific statutes to which each item relates: …."); 100.9710 (after quoting the IITA's definition of a "financial organization," the regulation states, "This definition constitutes an exclusive and exhaustive list of the types of organization which are 'financial organizations' under the Illinois Income Tax Act."). Since the lists set forth in this particular regulation are not similarly described as being exhaustive, they should, instead, be understood as being illustrative of the different types of expenses that either will or will not qualify for the training expense credit.

Since this dispute cannot be resolved by reference to the express terms of the Department's applicable regulation, that regulation must be considered in context with the statute it was promulgated to interpret. All creditable expenses under § 201(j) share attributes that are clearly set forth in the text of the statute itself. That is, the legislature has described creditable training expenses as "all amounts" that are: (1) paid or accrued; (2) on behalf of a taxpayer's Illinois employees or its employees who are residents of Illinois; (3) for educational or vocational training in semi-technical or technical fields or semi-skilled or skilled fields; and (4) deducted from gross income when computing taxable income. 35 **ILCS** 5/201(j). The applicable regulation further provides that certain expenses may qualify even if they are not direct costs of eligible training. 86 Ill. Admin. Code § 100.2150(d), (d)(1). One way of determining whether or not the expenses at issue here should qualify, therefore, is to determine whether the amounts are more like the indirect costs of training that the Department has acknowledged will qualify for the credit, or whether such expenses are more like the indirect costs the Department has announced will not qualify. *Compare* 86 Ill. Admin. Code § 100.2150(d)(1) *with* § 100.2150(d)(2).

Like the qualifying expense for compensation paid to eligible employees for the time spent in training, the amounts "Shanghai" paid for employee insurance (medical, dental and life), employee profit sharing, pension and stock retirement plans for the same period of time are clearly amounts that "Shanghai" paid "… on behalf of …" its eligible employees. 35 **ILCS** 5/201(j); Stip. ¶¶ 4-5, 12. After taking into consideration the Director's decision regarding the parties' cross-motions for summary judgment, I must point out that I am not concluding in this recommendation that the amounts "Shanghai" paid for pension, insurance and/or bonus contributions constitute compensation under

Illinois law. Rather, I am merely concluding that both types of expenses (compensation and the expenses being discussed here) are not, in fact, direct costs of training, and both expenses, in fact, provide clear benefits to the persons on whose behalf they are made. They cannot be understood as being anything but amounts that are "… paid or accrued *on behalf of* …" "Shanghai's" employees. 35 **ILCS** 5/201(j).

The parties also agree that "Shanghai" has not asked for a credit for all of its costs for employee insurance (medical, dental and life), employee profit sharing, pension and stock retirement plans. *See* Stip. ¶¶ 4-5, 12. Rather, the parties have stipulated that the amounts "Shanghai" claimed as creditable are limited to the amount of such expenses that are attributable to the amount of time "Shanghai's" eligible employees spent in eligible training. Stip. ¶ 5. In that respect, the expenses are also similar to the qualifying indirect costs of training that a taxpayer pays or accrues for compensation of, or reimbursement to, eligible employees and trainers, and/or for travel and/or lodging expenses for eligible employees for eligible training. 86 Ill. Admin. Code § 100.2150(d)(1)(A)-(C), (G)-(H). For example, a taxpayer's travel expense cannot be considered a "direct cost" of training, yet the applicable regulation states that such an expense qualifies for credit under § 201(j) of the IITA, if it was incurred to get an eligible employee to and/or from an eligible training program. 86 Ill. Admin. Code § 100.2150(d)(1)(H). "Shanghai's" employee insurance and pension amounts paid for the time its eligible employees spent in eligible training are also similar to the qualifying pro-rata amounts of rent a taxpayer pays for property for the amount of time the property is used for eligible training. 86 Ill. Admin. Code § 100.2150(d)(1)(E). That is to say, all such amounts are "… paid or accrued … *for* [eligible training] …" not because they are direct costs of training, but because they are

amounts paid on behalf of such employees, and because they are related or limited to the time such employees spend (or property is used) in eligible training. 35 **ILCS** 5/201(j).

The next expenses at issue are the amounts "Shanghai" paid for federal and state employer payroll taxes, which consist of "Shanghai's" federal and state unemployment taxes and its federal Social Security and Medicare taxes that were attributable to the days, weeks, or other periods during which its Illinois resident employees, or its employees who worked in Illinois, spent in qualified training. Stip. ¶¶ 4-5; Stip. Add. ¶ 1. Here again, the Department does not dispute that such amounts were, in fact, accurately calculated, that such amounts were related to the time "Shanghai's" eligible employees spent in eligible training, and/or that such amounts were deducted from gross income when computing "Shanghai's" taxable income. Stip. ¶¶ 4-5; Stip. Add. ¶ 1; 8/16/99 Agreed Order (¶ 7); Department's Brief, *passim*.

Notwithstanding the Department's failure to counter, or even address, "Shanghai's" argument that the expenses at issue were creditable under the plain text of the statute, I cannot agree with "Shanghai's" conclusion that the amounts it paid for employer payroll taxes are creditable, because none of those amounts are, nor can they reasonably be deemed to be, "… paid or accrued *on behalf of* …" "Shanghai's" eligible employees. 35 **ILCS** 5/201(j) (emphasis added). When rejecting "Shanghai's" conclusion that all of the amounts it claimed are creditable under the plain text of § 201(j), I am mindful that it is "Shanghai" who bears the burden to show entitlement to the statutory credit. Balla, 96 Ill. App. 3d at 296, 421 N.E.2d at 238. And when concluding that "Shanghai's" employer payroll taxes are not creditable under the plain terms of § 201(j), I also find it necessary to

consider the texts and effects of the federal and state statutes pursuant to which such taxes are paid.

Employer payroll taxes are imposed on employers, not employees.[6] Specifically, § 3111(a) of the IRC imposes an "Old age, survivors and disability insurance [also known as Social Security] tax on employers." 26 U.S.C. § 3111(a). That section specifically provides, "In addition to other taxes, there is hereby imposed on every employer an excise tax, with respect to having individuals in his employ, equal to the amount following percentages of the wages … paid by him with respect to employment …." *Id.* Section 3111(b) of the Code imposes a "Hospital [also known as Medicare] tax on employers." 26 U.S.C. § 3111(b). That section specifically provides that, "In addition to other taxes, there is hereby imposed on every employer an excise tax, with respect to having individuals in his employ, equal to the amount following percentages of the wages … paid by him with respect to employment …." *Id.* Section 3301 of the Code describes the "Rate of [Federal Unemployment] tax" which, in turn, "… is hereby imposed on every employer (as defined in section 3306(a)) for each calendar year an excise tax, with respect to having individuals in his employ, …." 26 U.S.C. § 3301. Section 1400 of Illinois' Unemployment Tax Act describes the rate of Illinois unemployment tax contributions that are imposed on employers. 820 **ILCS** 405/1400. Specifically, that section provides that "… For the year 1941 and for each calendar year thereafter, [Illinois unemployment tax] contributions shall accrue and become payable by each employer upon the wages paid with respect to

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6 In the [ALJ's Recommended] Order Regarding the Parties' Cross-Motions for Summary Judgment, this writer mistakenly concluded that "Shanghai's" payroll taxes consisted of taxes that were imposed on "Shanghai's" employees, and withheld by "Shanghai". *See* [ALJ's Recommended] Order Regarding the Parties' Cross-Motions for Summary Judgment, p. 19; *see also* 26 U.S.C. §§ 3101(a)-(b), 3102(a). That conclusion was an error of fact and of law, and the error was made plain by the parties' Stipulation Addendum ¶ 1.

employment after December 31, 1940. … Such contributions shall not be deducted, in whole or in part, from the wages of individuals in such employer's employ. ***." *Id.*

After taking into account the nature and purpose of federal and state employer payroll taxes, I conclude that such amounts are not part of "… all [of the] amounts ["Shanghai"] paid or accrued *on behalf of [its eligible employees*] …." *Compare* 35 **ILCS** 5/201(j) (emphasis added) *with* 26 U.S.C. §§ 3111(a)-(b), 3301; *and* 820 **ILCS** 420/1400. Rather, it is clear that "Shanghai" paid such amounts on its own behalf. 26 U.S.C. §§ 3111(a)-(b), 3301; 820 **ILCS** 420/1400. Since such amounts do not satisfy one of the plain and clear terms of § 201(j), they are not creditable. Thus, "Shanghai" has not satisfied its statutory burden to show that these particular expenses are creditable under that statutory provision. Balla, 96 Ill. App. 3d at 296, 421 N.E.2d at 238.

On the other hand, I conclude that "Shanghai" has rebutted the Department's determination that the amounts it paid for employee insurance (medical, dental and life), employee profit sharing, and for pension and stock retirement plans that are attributable to the days, weeks, or other periods during which its Illinois resident employees, or its employees who worked in Illinois, spent in eligible training, are not creditable under § 201(j). All such amounts are clearly paid or accrued on behalf of "Shanghai's" employees, and, since the expenses are limited to the time "Shanghai's" eligible employees spent in eligible training, they are also paid or accrued for eligible training. *See* Stip. ¶¶ 4-5, 12. As required by § 201(j), such amounts are part of "… all [of the] amounts ["Shanghai"] paid or accrued on behalf of … [eligible employees and] for … [eligible training]." 35 **ILCS** 5/201(j). It is also undisputed that such amounts were deducted from gross income when "Shanghai" calculated taxable income. *See* Stip. ¶¶ 1, 3-12; Department's Brief, pp. 32-34;

8/16/99 Agreed Order (¶ 7). Those amounts, therefore, should be allowed as creditable training expenses, under the plain and clear text of § 201(j). 35 **ILCS** 5/201(j). Additionally, such amounts are more like the indirect training costs that the Department has said will qualify for the credit, than those indirect costs that the Department has said will not qualify. 86 Ill. Admin. Code § 1000.2150(d)(1)-(2).

Other Issues

As part of their pre-hearing order, the parties raised other issues to be resolved at hearing. All other such issues were related to the FSC or 80/20 issue. Because I have concluded that, in this case, there is no factual or statutory bases for reallocating "Shanghai's" payroll and/or property to "STCI" for purposes of the 80/20 test, such issues are either impliedly resolved in favor of "Shanghai" (with regard to whether there is a factual basis for the Department's combination of "STCI" within "Shanghai's" Illinois unitary business group) or are rendered moot. *See* Prehearing Order. Therefore, I am including no further conclusions regarding those issues.

Conclusion

I recommend that the Director reconsider the composition of "Shanghai's" Illinois unitary group as determined by the Department following audit, and that he eliminate "STCI" from that group. Any tax liabilities that may have been proposed as a result of "STCI's" combination into "Shanghai's" group should be eliminated.

I also recommend that the Director revise the Department's prior denials of "Shanghai's" amended returns so as to grant "Shanghai" the statutory credit for the pro-rata amounts that "Shanghai" paid or accrued for employee insurance (medical, dental and life), employee profit sharing, pension and stock retirement plans for the time its eligible

employees spent in eligible training. With regard to "Shanghai's" claim that the pro-rata amounts it paid in employer payroll taxes, however, the Department's prior denials should be finalized.

I note that, because of the parties' stipulated record in this case, the effect of denying "Shanghai's" claim for credit for the pro-rata amount of its employer payroll taxes while granting its claim for other expenses is to reduce the percentage of Fringe Benefits vis-a-vis its Illinois Payroll. TMSJ Ex. A-2; *see also* Stip. ¶¶ 4-5. Specifically, when "Shanghai's" employer payroll taxes attributable to its Illinois employees are subtracted from its total Fringe Benefits for the same location, the new Fringe Benefits percentage figure will be 21.75%. TMSJ Ex. A-2;[7] *see also* Stip. ¶¶ 4-5. The amount of "Shanghai's" creditable training expenses attributable to Fringe Benefits should be calculated as 21.75% of the amount the Director previously granted as creditable Trainee Wages. Stip. ¶¶ 12; *see also* TMSJ Ex. A (¶ 19). When added together with the expenses "Shanghai" paid as Trainee Wages, previously determined to be creditable pursuant to the Director's prior grant of partial summary judgment for "Shanghai", the total creditable training expenses granted should be as follows:

Tax Year	Trainee Wages (previously approved)	Fringe Benefits (Trainee Wages – 21.75%)	TOTAL
1992	$ 252,154	$ 54,843	$ 306,997
1993	262,297	57,050	319,347
1994	303,595	66,032	369,627
TOTAL	$ 818,046	$ 177,925	$ 995,971

[7] That 21.75% figure is reached after performing the following calculations using the amounts "Shanghai" used when calculating the percentage of Fringe Benefits per Annual Payroll. TMSJ Exs. A (¶ 12), A-2 (column 1 amounts) (noted *supra*, pp. 12-13 n.1); *see also* Stip. ¶¶ 4-5, 57; 8/16/99 Agreed Order (¶ 7). First, "Shanghai's" Illinois Payroll Taxes must be subtracted from its Total Fringe Benefits for the same area, or 286,356 – 75,237 = 211,119. *See* TMSJ Ex. A-2 (column 1 amounts for rows 5 (Payroll Taxes) and 12 (Total Fringe Benefits)). That difference represents the revised Total Fringe Benefits. Then, the revised Total Fringe Benefits amount must be divided by the Annual Payroll, or 211,119 / 970,523 = 21.75%. *See id*. (column 1, row 14).

Stip. ¶¶ 8-9, 12; TMSJ Ex. A (¶ 19); 8/16/99 Agreed Order. Interest for the amounts of creditable training expenses granted should be computed and paid to "Shanghai", pursuant to statute. 35 **ILCS** 5/909(c).

Date: 2/7/2002

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Administrative Law Judge